LIBRARY
SUPREME COURT, U. S.

FILED
JUL 5 1975
MICHAEL RODAK, JR., CLERK

In The

Supreme Court of the United States

OCTOBER TERM, 1974

No. 75-27

ABRAHAM GRUNIN,

Petitioner,

v.

INTERNATIONAL HOUSE OF PANCAKES
a division of
INTERNATIONAL INDUSTRIES, INC.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

JAY S. FICHTNER
BERMAN, FICHTNER & MITCHELL
2650 LTV Tower
1525 Elm Street
Dallas, Texas 75201
A/C 214: 748-9911
Attorneys for Petitioner

Of Counsel:
DOUGLAS E. YEAGER
2650 LTV Tower
Dallas, Texas 75201

SOUTHWESTERN LAW PRESS — DALLAS, TEXAS — (214) 742-4257

TABLE OF CONTENTS

Page

Opinions Below 2

Jurisdiction 2

Questions Presented 2

Constitutional and Statutory Provisions Involved 4

Statement of the Case 5

Reasons for Granting Writ 8

1. The Decision of the Court of Appeals, That the Class Action Settlement Notice Satisfied Due Process Requirements of the Fifth Amendment and Rule 23(e) As to Time and Content, Conflicts with Decisions of the Supreme Court and Other Courts of Appeals 8

2. The Court of Appeals Erroneously Binds Petitioner and Other Franchisees by Res Judicata to Cooperate with Respondent in Continuing Violations of the Sherman Anti-Trust Act, 15 U.S.C. §§ 1 and 2 13

3. The Supreme Court Has Not Yet Addressed Itself to the Question of Whether "Coercion" Is An Element of Proof in a Private, Injunctive and Treble Damage Class Suit Where Unlawful Ties in a Franchise Industry Are at Issue, Although There Are Conflicting District Court and Court of Appeals Decisions 18

4. The Trial Court Exceeded Its Power and Violated Petitioner's and Other Franchisees' Freedom of Contract-Right As Protected by the Due Process Clause of the Fifth Amendment by Its Ipso Facto Reformation of the Franchise Agreements, Without Prior Individual Consent 21

Page

5. Legal Ethics and Public Policy Preclude, and the Conscience Is Shocked by, an A Priori Written Stipulation in a Class Action Settlement Agreement As to the Amount and Mechanics of Distribution of Legal Fees to be Paid to Plaintiffs' Attorneys Upon Its Approval by the Court 25

Conclusion 28

Appendix

Cases: Page

Airline Stewards v. American Airlines, Inc., 455 F.2d 101 (7th Cir. 1972) 12

Armstrong Cork Co. v. Lyons, 366 F.2d 206 (8th Cir. 1966) 24

Central Specialties Co. v. Schaefer, 318 F.Supp. 855 (N.D. Ill. 1970) 24

Chock Full O'Nuts Corp., Trade Reg. Rep., ¶ 20,441 (F.T.C. 1973) 16, 17

City of Detroit v. Grinnell Corp., 495 F.2d 448, (2nd Cir. 1974) 25

Eisen v. Carlisle & Jacquelin, 417 U.S. 134 (1974) 8, 11, 12

Federal Trade Commission v. Texaco, Inc., 393 U.S. 223 (1968) 18, 19

Freeman v. Ryan, 408 F.2d 1204 (D.C. Cir. 1968) 25

Greenfield v. Villager Industries, 483 F.2d 824 (3rd Cir. 1973) 8, 10, 11, 13

Hedges v. Dixon County, 150 U.S. 182 (1893) 24

In Re International House of Pancakes Franchise Litigation, 1973-2 Trade Cases ¶ 74,616 (W.D. Mo.), aff'd. 487 F.2d 303 (8th Cir. 1973) 2

International Salt Co. v. United States, 332 U.S. 392 (1947) 16

Kugler v. AAMCO Transmissions, Inc., 460 F.2d 1214 (8th Cir. 1972) 17

Lamb v. United Security Co., 59 F.R.D. 25 (S.D. Iowa 1972) 12

Manufacturers' Finance Co. v. McKey, 294 U.S. 442 (1935) 24

Milone v. English, 306 F.2d 814, (D.C. Cir. 1962) 25

Milstein v. Werner, 57 F.R.D. 515 (S.D. N.Y. 1972) 8, 9, 12

Page

Milwaukee Towne Corp. v. Loew's, Inc., 190 F.2d 561 (7th Cir. 1951), cert. denied, 342 U.S. 909 (1952) 25, 26

Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306 (1950) 8, 11, 13

Northern Pacific Ry. Co. v. United States, 356 U.S. 1 (1958) 14, 15

Perma Life Mufflers, Inc. v. International Parts Corp., 392 U.S. 134 (1968) 19

Siegal v. Chicken Delight, Inc., 448 F.2d 43 (9th Cir. 1971), cert. denied, 405 U.S. 955 (1972) 15, 16, 17

Sprague v. Ticonic National Bank, 307 U.S. 161 (1939) 26

State of Illinois v. Harper & Row Publishers, Inc., 55 F.R.D. 221 (N.D. Ill. 1972) 26

Steffen v. United States, 213 F.2d 266 (6th Cir. 1954) 24

Susser v. Carvel Corp., 332 F.2d 505 (2nd Cir. 1964), cert. denied, 381 U.S. 125 (1965) 17

Sylvan Beach v. Koch, 140 F.2d 852 (8th Cir. 1944) 23

Times-Picayune Publishing Co. v. United States, 345 U.S. 594 (1953) 15

Trustees v. Greenough, 105 U.S. 527, 26 L.Ed 1157 (1881) 25

Ungar v. Dunkin' Donuts, Trade Reg. Rep., ¶ 60,361 (E.D. Pa. 1975) 17, 18, 19, 21

United States v. Loew's, Inc., 371 U.S. 38 (1962) 15

United States v. Paramount Pictures, Inc., 334 U.S. 131 (1948) 15

United Transportation Union v. State Bar of Michigan, 401 U.S. 581 (1971) 24

Page

Windsor v. McVeigh, 93 U.S. 274, 23 L.Ed. 914 (1874) 24

United States Constitution:

Amendment V 4

Statutes:

Clayton Anti-Trust Act:
15 U.S.C. § 14 ..... 4, 23, 24
15 U.S.C. § 15 ..... 5, 24
15 U.S.C. § 26 ..... 5, 24

Federal Rules of Civil Procedure:
Rule 23(e) 5, 8, 9

Judiciary and Judicial Procedure:
28 U.S.C. § 1254(1) 2

Sherman Anti-Trust Act:
15 U.S.C. § 1 ..... 3, 4, 13, 18, 23, 24
15 U.S.C. § 2 ..... 3, 4, 13, 18, 23, 24

Procedural Manual:

Manual for Complex Litigation 27

Secondary Material:

Code of Professional Responsibility
Canon 5 26

In The

Supreme Court of the United States

OCTOBER TERM, 1974

No. .....

ABRAHAM GRUNIN,

Petitioner,

v.

INTERNATIONAL HOUSE OF PANCAKES
a division of
INTERNATIONAL INDUSTRIES, INC.,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

Abraham Grunin, Petitioner, respectfully prays that a Writ of Certiorari issue to review the Judgment and Opinion of the United States Court of Appeals for the Eighth Circuit entered in this proceeding on March 17, 1975, which affirmed a Judgment of the United States District Court for the Western District of Missouri* on November 29, 1973.

* Because of the extraordinary length of the settlement agreement, its full exposition is not set forth herein but may be found in "Joint Appendix, Volume I" at 438-556 filed herein.

OPINIONS BELOW

The Opinion of the United States Court of Appeals for the Eighth Circuit is reported at 513 F.2d 114 (A-1). The Judgment approving the Class Settlement Agreement, out of which this Petition arises, was without opinion, and therefore is not reported (A-31). A prior opinion of the United States Court of Appeals for the Eighth Circuit in this same litigation affirming a judgment by the United States District Court for the Western District of Missouri rejecting a prior, almost identical class action settlement is reported at 487 F.2d 303 (A-40), and the opinion of the United States District Court rejecting the same settlement agreement is reported in 1973-72 Trade Cases, ¶ 74,616 (A-43).

JURISDICTION

On March 17, 1975, the Court of Appeals entered its Judgment (A-28) and on April 8, 1975, it entered its Order Overruling Petitioner's Motion for Rehearing (A-30). Jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

QUESTIONS PRESENTED

(1) Whether the allowance of nine (9) days to object to a proposed class action settlement fulfills the due process requirement that an interested party be afforded a reasonable time rationally to decide whether to appear and object, default or otherwise make his views known.

(2) Whether a class action settlement agreement which requires that the franchisees of a fast food franchise chain, in order to retain their franchises, purchase their flour and ac-

counting services and lease their restaurant equipment from the franchisor, *per se* violates the Sherman Anti-Trust Act, 15 U.S.C. §§ 1 and 2.

(3) Whether interposition by a franchisor as its primary defense to a class action suit for treble damages and injunctive relief that it practiced no individual coercion to induce its franchisees to lease from franchisor their restaurant equipment, precludes a finding of *per se* illegal tying arrangements proscribed by the Sherman Anti-Trust Act, 15 U.S.C. §§ 1 and 2.

(4) Under the guise of approving settlement of a class action brought for recovery of treble damages and injunctive relief, did the trial court exceed its judicial power by disregarding the Complaints on file and Notice of Class Action Designation and entering a judgment materially and substantively reforming the franchise contract documents without first obtaining the consent of each class member affected thereby?

(5) Whether written stipulations in the class action settlement agreement that One Million Two Hundred Fifty Thousand Dollars ($1,250,000.00) was a just and reasonable fee to be paid to class plaintiffs' attorneys and as to the manner in which such sum was to have been paid created such an appearance of conflict of interest that the motives of counsel who negotiated and proposed such settlement for approval might be called into question and such doubt cast upon the traditionally sacred relationship of attorney-client that the entire class settlement should be invalidated as contrary to public policy.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Constitution of the United States:

Amendment V.
"No person shall . . . be deprived of life, liberty, or property, without due process of law . . ."

Statutes:

Sherman Anti-Trust Act.

15 U.S.C. § 1.

"Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States . . . is hereby declared to be illegal . . ."

15 U.S.C. § 2.

"Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States . . . shall be deemed guilty of a felony . . ."

Clayton Anti-Trust Act.

15 U.S.C. § 14.

"Section 3. It shall be unlawful for any person engaged in commerce . . . to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies, or other commodities . . . on the condition, agreement, or understanding that the lessee or purchaser thereof shall not use or deal in the goods, wares, merchandise, machinery, supplies, or other commodities of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, or contract for sale or such condition, agreement, or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce."

15 U.S.C. § 15.

"Section 4. Any person who shall be injured in his business or property by reason of anything forbidden in the anti-trust laws may sue therefor in any District Court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee."

15 U.S.C. § 26.

"Section 16. Any person, firm, corporation, or association shall be entitled to sue for and have injunctive relief . . . against threatened loss or damage by a violation of the anti-trust laws . . ."

Rule 23(e), Federal Rules of Civil Procedure.

"A class action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to all members of the class in such manner as the court directs."

STATEMENT OF THE CASE

Prior to 1968, when the first of the suits was filed, which ultimately gave birth to the class action multi-district litigation out of which this Petition arises, the printed, standard, fifteen-year franchise agreements of International House of Pancakes (IHOP), a fast food franchisor, required its restaurant franchisees to: (1) lease from IHOP all of their furniture, fixtures and equipment for not less than fifteen years; (2) buy from IHOP all of their dry mixes at fixed prices; (3) buy all of their paper products from IHOP at its fixed prices; (4) place all their insurance through IHOP; (5) place all of their advertising through IHOP; (6) purchase all accounting services from IHOP; (7) lease their land and building from IHOP. In addition, and

for the privilege of obtaining the license to use the IHOP name, trade-mark and logos, they paid upwards of $45,000.00 (R.A. 73-90).[1]

On October 26, 1971 the trial court entered its Class Action Order creating a Class composed of those franchisees who were then operating franchised restaurants and a second class composed of former franchisees who no longer were operating IHOP restaurants (R.A. 125-127). On November 19, 1971, the court notified all those interested of the pendency of "actions for treble damages and injunctive relief for alleged violations of anti-trust laws of the United States" (R.D. 8).[2]

A first proposed settlement agreement in the class actions was heard by the Court on June 1st and 2nd, 1973, following certified mail notices sent to class members on April 27, 1973, (R.A. 128-136). The notices contained the advice, among other things, that Plaintiffs' counsel would file a petition for allowance of aggregate counsel fees in the amount of $1,110,000.00 (R.A. 128). To each mailed notice was appended a complete copy of the proposed settlement agreement, which subsequently was disapproved by the Court on July 12, 1973 (A-43). IHOP's appeal from the disapproval was summarily rejected on November 2, 1973 (A-40).

On Friday afternoon, November 9, 1973, notice of a second, proposed settlement agreement of the class actions was mailed by the Clerk of Court, this time advising among other things, that $1,250,000.00 had been *set aside* as an aggregate sum for Plaintiffs' attorneys' legal fees (R.D. 28, R.A. 563-569). No

[1] "R.A." Citations are to pages of the printed Appendix filed in the Court below which is a part of the certified record filed in this cause.

[2] "R.D." Citations are to pages of the docket entries filed in the Court below which are part of the certified record in this cause.

copies of the second, proposed settlement agreement were attached to the November 9, 1973, notices, which also directed that a hearing on the settlement agreement would be held before the Court on November 28th and that all those who wished to appear in opposition to the proposal were to have notices of appearance on file with the Court no later than November 23rd (R.A. 560-569).

Petitioner appeared and vociferously objected to the settlement agreement during the court hearing which took place on November 28th and 29th, and although neither monetary damages nor injunctive relief was granted to the major class of current franchisees, the court approved the settlement on November 29th (A-31).

Immediately upon declaring its approval of the settlement agreement from the bench, the Court launched upon a hearing of testimony on the several applications for legal fees that had been filed, and on February 1, 1974, after Petitioner had filed his Notice of Appeal, it distributed the entire sum of $1,250,000.00 among all of the Plaintiffs' attorneys', but excluded a distribution to Petitioner's counsel (R.A. 1316-1324).

The settlement agreement approved by the trial court and the Court of Appeals provides neither injunctive relief against IHOP nor monetary damages to class members, treble or otherwise, as sought in the Complaints on file and as evidenced in the Notice of Designation of Class Action. On the contrary, it requires Petitioner and other franchisees in order to retain their franchises to purchase all of their dry mixes from IHOP; requires them to lease all of their restaurant equipment, furniture and

fixtures from IHOP; and requires them to pay for accounting services provided by IHOP whether desired or not (R.A. 502-503; 449-459; 485-487).

Petitioner, Abraham Grunin files this Petition for Certiorari to review the adverse decisions of the Courts below.

REASONS FOR GRANTING THE WRIT

1. THE DECISION OF THE COURT OF APPEALS, THAT THE CLASS ACTION NOTICE SATISFIED DUE PROCESS REQUIREMENTS OF THE FIFTH AMENDMENT AND RULE 23(e) AS TO TIME AND CONTENT, CONFLICTS WITH DECISIONS OF THE SUPREME COURT AND OTHER COURTS OF APPEALS.

Rule 23(e) requires that notice of a proposed dismissal or compromise of a class action be given to *all* members of the class. Rule 23 Notices must conform to the requirements of due process of law in order to fairly insure the protection of the interests of absent parties who are to be bound by the judgment. *See, e.g., Eisen v. Carlisle & Jacquelin,* 417 U.S. 134 (1974).

Notice of a proposed class action settlement "must afford a reasonable time for those interested to make their appearance." *Mullane v. Central Hanover Bank & Trust Co.,* 339 U.S. 306, 314 (1950). The Third Circuit Court of Appeals in synthesizing the language of this court in *Mullane* held that Rule 23 Notices to class members must "afford a reasonable time for those interested to choose whether to appear or default, acquiesce or contest." *Greenfield v. Villager Industries,* 483 F.2d 824, 834 (3rd Cir. 1973). *See also, Milstein v. Werner,* 57 F.R.D. 515 (S.D. N.Y. 1972).

In direct violation of the due process requirement that absent class members be afforded a reasonable time to choose whether to accept or contest a proposed class action settlement, the Court below held that the allowance of only nine (9) working days was sufficient for class members to retain counsel, obtain a copy of the copious agreement, read and digest its significance and "rationally decide whether they should intervene in the settlement proceedings or otherwise make their views known." *Milstein, supra,* at 518.

The Rule 23(e) Notice of the proposed settlement at bar, mailed at 4:00 P.M. on Friday, November 9th, comprised a seven (7) page summary of a 119 page settlement and stated that those who chose to object to the settlement agreement were to have filed a written appearance in the District Court at Kansas City on or before Friday, November 23, 1973 (R.D. 28; R.A. 560-569). The period between November 9 and November 23 included two weekends and the Thanksgiving holiday. Class members thus were allowed only nine (9) working days to make a decision, based upon an abbreviated summary of a complex settlement agreement, whether to contest it.[3] The nine day period was totally insufficient for class members, scattered as they are across the nation, to receive the notice by mail, study the proposal, acquire a copy of the settlement

[3] To add further confusion and create further time pressures, the Court issued a second notice to class members a week later, on Friday, November 16th, amending the November 9th notice and creating additional, specific decisions to be made, while exhorting and admonishing the class members to "act quickly as this opportunity will not be available after entry of judgment," presumptively November 28th. (R.D. 28; R.A. 575).

agreement by mail,[4] obtain independent counsel to evaluate the complex document,[5] rationally decide whether to travel to Kansas City to object to the settlement, formulate objections to the settlement, and file written notice of appearance by mail. The nine day period was patently unreasonable and as "fatal to due process as no notice at all." [6] *Greenfield, supra,* at 834.

The Court below opined that class members were not deprived of due process by reasoning that the length of time the litigation had been ongoing was "highly relevant" and that some of the class members were represented by personal counsel at a prior settlement hearing and accordingly the class had "continuing notice" sufficient to satisfy due process requirements, which is a completely novel and heretofore unespoused doctrine. Even assuming that counsel for some of the individual class members had been kept informed of the settlement negotiations, of which Petitioner denies knowledge, "continuing notice" to *some* members of the class provides no due process protection to the vast remainder of class members. This "continuing notice" theory is without precedent and if followed to its logical end leads to the conclusion that "no notice at all,

[4] The Court below held that "class members are not expected to rely upon the notices as a complete source of settlement information." (A-11).

[5] Since the settlement agreement stipulated that $1,250,000 was a fair and reasonable legal fee to be paid to class counsel and it was the same class counsel together with defense counsel who were recommending the agreement for approval, it is doubtful that class members would have been given information about the agreement with any degree of objectivity.

[6] The deprivation of due process practiced upon class members by the inadequacy of time is evidenced by the appearance of nine (9) class members as *amici curiae* in the Court below asserting that the period of time allowed by the notices was so short that they did not have an opportunity to make known to the trial court their objections to the settlement. (A-6).

published or otherwise, would be required in the present case." *Eisen, supra,* at 177. The unambiguous requirement of Rule 23(e) is that *"all members of the class" shall be given notice of a proposed compromise of a class action,* not just those with individual counsel, who had appeared at a prior hearing at which a settlement had been rejected. The decision of the Court below in approving a constitutionally inadequate notice procedure is in clear conflict with *Mullane, Eisen,* and *Greenfield.*

The notices also founder on the shoals of objectivity and neutrality in their abbreviated outline of the complicated, extraordinarily long and confusing settlement provisions. While exalting, for example, alleged "aggregate savings" to the class of between $12 Million and $20 Million and the benefits of equipment "ownership" under any one of four (4) option revisions to the equipment lease, it omits mention that all of the equipment is pledged to banks to secure IHOP's enormous indebtedness and therefore could not be sold, encumbered or removed without prior release of such indebtedness. The notice creates the spectre of defeat, while ignoring almost certain victory on issues relating to menu price-fixing; required purchases of insurance, accounting services and paper products from IHOP; admitted, clandestine "kick-backs" that IHOP had been taking for many years.

In short, the Notice was intended as a "selling job" to the franchisees[7] in furtherance of which it contains out-right mis-

[7] The notice argues as follows: "It is quite possible that a trial of this lawsuit will result in a judgment for defendant; and the franchisees will recover nothing and also lose the extensive benefits they would otherwise receive under the proposed settlement * * * [T]he proposed settlement provides immediate available relief to the franchisees which represents a very large part of the maximum relief they could hope to

representations of facts, misleading constructions of the contractual provisions, erroneous, self-serving legal conclusions, and it omits stating material facts which necessarily should have been disclosed so as to make the facts as stated true under the surrounding circumstances. Traditional fair play demands scrupulous neutrality in the presentation of the settlement agreement to class members so that their ultimate actions with regard to it are "rationally decided." *See, Airline Stewards v. American Airlines, Inc.*, 455 F.2d 101, 108 (7th Cir. 1972); *Milstein, supra,* at 518.

Finally, the record reveals that of the 310 class members, 109 did not even receive the notice. *Eisen* requires that notice must be sent to all class members "who can be identified through reasonable effort." While the notice was mailed to the last known addresses of class members, the record fails to indicate that any prior effort, reasonable or otherwise, was made to locate mis-addressed class members. Yet, after the settlement hearing, Liaison Counsel admitted locating additional class members. Under this Court's reasoning in *Eisen*, Rule 23 and procedural due process are not satisfied by the mere gesture of depositing notices in the mails to last known addresses. Furthermore, the trial court and counsel ignored the monitoring protection approved in *Lamb v. United Security Co.*, 59 F.R.D. 25, 42 (S.D. Iowa 1972), which requires that if a significant number of notices are not delivered, the court must revisit the

---

footnote 7, continued

obtain in the event of complete and total victory. The immediacy and certainty of the relief afforded, in the opinion of counsel signatory hereto, far outweighs any possible extra benefits of trial and doubtful results" (R.A. 567).

matter "to determine if further notice" would be required. Certainly 109 out of 310 class members deprived of any notice whatsoever of the settlement is a significant number.

The class action "procedure can be tolerated, if not completely justified, only if there is a fealty to both the spirit and the letter of the procedural rules, especially those relating to notice." *Greenfield, supra,* at 831-832. There was fealty to neither the spirit nor the letter of the procedural rules relating to notice in this class action. Class members in the case at bar suffered in terms of notice time, notice content, and reasonable effort to locate class members. Notice was a mere gesture. In the words of this Honorable Court:

> "When notice is a person's due, process which is a mere gesture is not due process." *Mullane, supra,* at 315.

This Honorable Court should grant its writ to correct the deprivation of due process approved by the Court below and settle these important questions of constitutional safeguards in connection with the settlement of class actions.

2. THE COURT OF APPEALS ERRONEOUSLY BINDS PETITIONER AND OTHER FRANCHISEES BY *RES JUDICATA* TO COOPERATE WITH RESPONDENT IN CONTINUING VIOLATIONS OF THE SHERMAN ANTI-TRUST ACT, 15 U.S.C. §§ 1 AND 2.

The settlement agreement approved by the Courts below contains and perpetuates *per se* illegal tying arrangements proscribed by the Sherman Anti-Trust Act, 15 U.S.C. §§ 1 and 2. In approving this settlement agreement, they have embraced and approvingly given *res judicata* effect to an agreement

violative of the anti-trust statutes, even though this Court has forcefully condemned such agreements "because of their pernicious effect on competition and lack of any redeeming virtue." *Northern Pacific Ry. Co. v. United States*, 356 U.S. 1, 5 (1958). This Court should grant its Writ in this cause to correct the lower court's error in having become the unwitting parties to an illegal agreement which "serve[s] hardly any purpose beyond the suppression of competition" and which ultimately results in economic loss to the general public as well as the franchisees.[8] *Northern Pacific, supra,* at 6.

The settlement agreement provides that to retain his license to use the IHOP name, trademark and method of business, the franchisee must purchase all of his pancake and waffle mix from Respondent,[9] must purchase his accounting services from

[8] The Trial Court recognized the impropriety of a court approving an illegal contract in its rejection of a prior, almost identical, proposed settlement of this cause.

> "If this court approved this proposed settlement, it would give judicial approval to the exact provisions of these franchise agreements, which plaintiffs have vigorously contended violated the anti-trust laws . . . . In addition, the members of the class would be bound, by judicial decree, to continue making these payments for the balance of a twenty-year lease (in most cases at least fifteen years), whereas, the franchisees who are not in the class would be free to seek injunctive relief against continued payments." (A-45).

Similarly, the Eighth Circuit Court in affirming the trial court recognized the same impropriety as follows:

> "In view of the fact that . . . it [the settlement] would continue in effect the very provisions of the franchise agreement challenged as violative of the anti-trust laws, we think Judge Collinson properly exercised his discretion in disapproving the settlement."(A-42).

Both Courts ignored their prior Opinions in approving this settlement which contains almost the same provisions as the prior proposed settlement.

[9] Though IHOP does not manufacture the mixes but merely designates a miller and provides the recipe to the miller, the settlement provides that the franchisees must purchase the mixes through IHOP at a price fixed by the settlement guaranteeing IHOP a "net profit" of 50% on all mixes sold (R.A. 502).

Respondent,[10] and must lease or purchase all of his restaurant equipment from Respondent (R.A. 438-556). Prior to the settlement agreement, each of these requirements was a condition to the franchisee's original purchase of the franchise license and was embodied in the standard, printed form franchise agreements which the record shows were never varied. These agreements from their inception and as continued and perpetuated by the settlement agreement contain all three of the elements, which together give rise to *per se* Sherman Anti-Trust violation.

First, there is a tied product which must be purchased in order to purchase and retain the tying product. Here the franchisees are required to purchase mixes, accounting services, and restaurant equipment, among other things, (tied products) as a condition of being allowed to purchase and retain the franchise license (tying product). Hence, the two-product test is satisfied. *See, Times-Picayune Publishing Co. v. United States*, 345 U.S. 594, 613-614 (1953).

Second, the tying product (license to use the IHOP trademark) possesses sufficient economic power to restrain competition in the tied product market. *Northern Pacific, supra*, at 6. When the tying product is patented, copyrighted, or a trademark, economic power is to be presumed. *United States v. Loew's, Inc.*, 371 U.S. 38, 45 (1962); *United States v. Paramount Pictures, Inc.*, 334 U.S. 131, 158 (1948); *Siegal v. Chicken Delight, Inc.*, 448 F.2d 43, 50 (9th Cir. 1971), *cert.*

[10]The settlement agreement continues unchanged in duration and amount the requirement that class members pay 5.2% or 6.2% of their gross receipts for accounting and management services, amounting to approximately $25,000 per year for each franchisee. (R.A. 756).

denied, 405 U.S. 955 (1972). Since the IHOP franchise license embodies a trademark, economic power must be presumed.

Finally, a "not insubstantial" amount of commerce must be affected by the agreement. *International Salt Co. v. United States*, 332 U.S. 392 (1947). The Respondent has conceded that this requirement is satisfied in this case.

While the decision in the Eighth Circuit below recognizes that the Court ought not "lend its approval to any contract or agreement that violates the anti-trust laws", it holds that the terms of the settlement agreement were not violations of the anti-trust laws *per se*, on the illogical ground that "the issue of illegality was vigorously contested by the parties." (A-16). The Court, however, makes no analysis of the meritoriousness of the Respondent's contest of the illegality of the settlement agreement, merely being satisfied to conclude that because Respondent did not admit to the illegality of the settlement agreement, such illegality was not a legal certainty. (A-16).

The only "defenses" to the *per se* illegality of the settlement agreement (and *a fortiori* to the franchise agreements) raised by Respondent were (1) that the two-product test was not satisfied as to the equipment, mixes and accounting services due to their inseparability from the franchise license and (2) the franchisees were not "coerced" to lease their equipment from the franchisor, since it was merely "offered" to them (and coincidentally "accepted" by all of them). *Siegal v. Chicken Delight*, *supra*, at 49 and *Chock Full O'Nuts Corp.*, Trade Reg. Rep., ¶ 20,441 (F.T.C. 1973) have studied, discussed and rejected the raised "defense" of two-product deficiency as far as

the equipment and dry flour mixes are concerned, and if the hoary doctrine of *stare decisis* has any significance in our jurisprudence, such defense was not worthy of comment, much less the dignity of a rationale upon which the Court of Appeals excused patent anti-trust violations. Insofar as the "coercion" defense is concerned, there has been a divergency of opinion in the lower courts. Because of its importance, Petitioner makes a more detailed analysis of the defense, *infra*.

To justify Respondent's allegation that the "two-product" test for illegality was not satisfied, the Eighth Circuit relied on its own opinion in *Kugler v. AAMCO Transmissions, Inc.*, 460 F.2d 1214 (8th Cir. 1972), which runs contra to all other Courts of Appeals as well as the Federal Trade Commission which have held that "sale of a franchise license, with the attendant rights to operate a business in the prescribed manner and to benefit from the good will of the trade-name, in no way requires the forced sale by the franchisor of some or all of the component articles." *Siegal, supra*, at 49; *see, also, e.g., Susser v. Carvel Corp.*, 322 F.2d 505 (2d Cir. 1964), *cert. denied*, 381 U.S. 125 (1965); *Chock Full O'Nuts Corp., supra*. At the very least the *AAMCO* opinion is distinguishable since it was restricted to advertising service, such services being "inextricable from the trade-mark, franchise system and logo as it is the major vehicle for promoting them." *Ungar v. Dunkin' Donuts*, Trade Reg. Rep., ¶ 60,204, at 65,745-46 (E.D. Pa. 1975). Advertising services excepted, the applicable decisions of the courts uniformly hold that the two-product test is satisfied when the availability of a franchise license is conditioned

upon the purchase of other tied items and services from the franchisor.

The settlement agreement approved by the Courts below thus clearly contains *per se* illegal tying arrangements proscribed by §§ 1 and 2 of the Sherman Anti-Trust Act, and the defensive theory advanced by the Respondent that the "two-product" test is not satisfied is wholly without merit as a matter of law, and the court approved settlement erroneously binds Petitioner and other franchisees by *res judicata* to engage in continuing anti-trust violations.

3. THE SUPREME COURT HAS NOT YET ADDRESSED ITSELF TO THE QUESTION OF WHETHER "COERCION" IS AN ELEMENT OF PROOF IN A PRIVATE, INJUNCTIVE AND TREBLE DAMAGE CLASS SUIT WHERE UNLAWFUL TIES IN A FRANCHISE INDUSTRY ARE AT ISSUE, ALTHOUGH THERE ARE CONFLICTING DISTRICT COURT AND COURT OF APPEALS DECISIONS.

In holding that the "alleged illegality of the settlement agreement is not a legal certainty," the Eighth Circuit Court relied on the contention of Respondent that the franchisees were not "coerced" into agreeing to lease their equipment from Respondent and accordingly no illegal tie-in existed. This Honorable Court, however, "has not set forth a coercion requirement in the tying cases." *Ungar, supra,* at 65,752. In his comprehensive analysis of the relevant case law, Judge Becker recently rejected "the doctrine that individual coercion must be proved in order to establish an unlawful tie," relying principally on his interpretation of this Court's decision in *Federal Trade Com-*

mission v. Texaco, Inc., 393 U.S. 223 (1968) and *Perma Life Mufflers, Inc. v. International Parts Corp.*, 392 U.S. 134 (1968). Judge Becker reasoned that this Court's decisions require only a showing that economic power was used in the tying transaction. *Ungar, supra,* at 65,764. This use of economic power may be established as follows:

> "[1] By proof of a resolutely enforced company policy to persuade or influence franchisees to buy only from the franchisor or its designated sources, particularly (but in any event) where there is an unequal bargaining relationship between the parties, or
> "[2] by proof that large numbers of franchisees have accepted a burdensome or uneconomic tie." *Ungar, supra,* at 65,766."

The required use of economic power is established as a matter of law in this case, because the undisputed facts prove both of the above described factual situations. First, Respondent had a "resolutely enforced company policy to persuade or influence franchisees to buy only from the franchisor" as admitted by Al Lapin, Jr., President and Chairman of the Board of Respondent, as follows:

> "The franchise package was organized, in its totality, sublease the building, to rent the equipment, to adhere to the standard operating procedures in every way. Part of that was that he was going to lease the equipment from the parent company" (Deposition of Al Lapin, p. 97).

In an address to a meeting of security analysts, Lapin admitted that IHOP "turns away prospective franchisees who have the money for a franchise but lack the willingness to do the job the International Industries, Inc. way" (R.A. 121). Lapin further described to the analysts the "*four* areas of separate

recurring sources of revenue and profit to International" as follows:

> "The *first* is an override which we receive on the sublease of the restaurant building to the franchisee . . . .
>
> "Our *second* revenue source is in the leasing of all the trade fixtures and equipment.
>
> "The *third* area of recurring profit comes from quantity discounts on all franchise food purchases, direct sales of paper goods, chinaware and IHOP trademark items.
>
> "The *fourth* recurring source of profit is the service charge the franchisee pays to the company" (R.A. 123).

It thus was a studied, resolutely enforced policy for IHOP to "influence" franchisees to lease their equipment from the Respondent and "turn away prospective franchisees" who refused. Clearly there was an unequal bargaining relationship between the parties, since the prospective franchisee was an individual interested primarily in the IHOP trade-mark and method of operation while the Respondent-Franchisor was a multi-million dollar corporation holding the rights to the trade-mark. The first alternative method of proving the requisite economic power used in the tying transaction is demonstrated in the record as a matter of law.

The second method of proving the use of economic power is also satisfied in this case, since it is undisputed that "large numbers of franchisees accepted a burdensome or uneconomic tie." There are 310 class members all of whom accepted the tying of the equipment lease to the franchise license. It is further undisputed that the equipment lease is a burdensome and uneconomic tie, because a typical franchisee is required to pay a total of $241,200.00 in equipment lease payments over a

twenty-five year period for equipment which cost the franchisor in 1966 only $40,000.00 (R.A. 123 & 852).

The requirement that economic power be used in the tying transaction is thus satisfied as a matter of law under the undisputed facts of this case. The illegality *per se* of the settlement agreement cannot be disputed on the basis of an alleged absence of coercion. The relevant question is not whether there was cocercion, but whether economic power was used in the transaction. The requirement under the court approved settlement agreement that the franchisees lease or purchase all of their equipment from the franchisor is thus a *per se* illegal tying arrangement perpetuated.

Judge Becker has described the coercion doctrine in the law of anti-trust tying as "an increasingly important, yet relatively uncharted area of the law. The few guideposts that do exist stem from District Court opinions." *Ungar v. Dunkin' Donuts*, Trade Reg. Rep., ¶ 60,361, at 66,537 (E.D. Pa. 1975). This Court should grant its Writ to decide this important question of federal law which has not been, but should be, settled.

4. THE TRIAL COURT EXCEEDED ITS POWER AND VIOLATED PETITIONER'S AND OTHER FRANCHISEES' FREEDOM OF CONTRACT RIGHT AS PROTECTED BY THE DUE PROCESS CLAUSE OF THE FIFTH AMENDMENT BY ITS *IPSO FACTO* REFORMATION OF THE FRANCHISE AGREEMENTS, WITHOUT PRIOR INDIVIDUAL CONSENT.

The original, printed franchise documents are composed of a "Franchise Agreement," a "Sublease" (of land and building) and an "Equipment Lease" (of equipment, fixtures and signs)

comprising nine 8½" x 14" pages, exclusive of schedules (R.A. 73-84). The class settlement agreement approved by the Courts below comprise no less than 119 pages which substantively and materially modify and reform the mutual rights and obligations of the parties, including a long and complicated formula under which the franchisees purportedly have "options" to "purchase" their furniture, fixtures and equipment from IHOP, but which in no way otherwise relieves them of their obligations to lease and purchase their equipment from the franchisor (R.A. 449-459; 535-539). Although the franchisees allegedly have the "option" to "purchase" their equipment, if they exercise their "option" and "purchase" the equipment, they are specifically precluded from selling it, borrowing against it, removing it from the franchised premises or otherwise dealing with it as an "owner." Furthermore, the illegal tie in no way is dissolved, because if purchased, the equipment must be purchased from IHOP, and once purchased, the franchisees are obligated to "sell" it back to IHOP upon termination of the franchise license (R.A. 445-57). Furthermore, even if exercise of one of the options were to invest the franchisees with the ordinarily understood indicia of ownership, they would be illusory and hollow within the context of this case, because all of the furniture, fixtures and equipment, as well as the franchise agreements themselves and the subleases of land and building are pledged to secure a One Hundred Million Dollar obligation which IHOP has to a group of international banks (R.A. 898). One might even ask whether IHOP had the right to enter into such an arrangement or whether a gigantic fraud has been perpetrated upon the Class Members and the Court.

The settlement agreement also provides a complicated formula to determine the price which the franchisees must pay IHOP for their pancake and waffle dry mixes, but again in no way does it relieve them of their obligation to purchase such pancake and waffle dry mixes from IHOP (R.A. 502). In addition, the settlement documents, instead of granting monetary mollification for past damages and injunctive relief against future abuse, modify and reform the existing rights and obligations between the parties as to the purchase of silverware, chinaware, paper and other items; purchase of advertising; as to forfeiture of the restaurant license if the franchisee becomes more than two weeks in default of payments to IHOP; as to the accounting for, and crediting of, weekly payments which the franchisees are obligated to make to the franchisor.

Plaintiffs' Complaints prayed for treble damages and injunctive relief under §§ 1 and 2 of the Sherman Act and § 3 of the Clayton Act, yet the trial court approved a settlement agreement totally devoid of any of the relief prayed for and adopted as its judgment closing the case a result which effectively permits IHOP to retain its pilfered loot.

Petitioner respectfully submits that the trial court's act in modifying and reforming the contractual rights and obligations between the Plaintiff-Franchisees and the Defendant-Franchisor, a result neither contemplated nor sought, constituted excessive imposition of judicial power and authority. The leading case of *Sylvan Beach, Inc. v. Koch,* 140 F.2d 852, 861 (8th Cir. 1944) holds that "A court may not, without the consent of all persons affected, enter a judgment which goes beyond the claim asserted in the pleadings. Unless all parties in interest are in

court and have voluntarily litigated some issue not within the pleadings, the court can consider only the issues made by the pleadings, *and the judgment may not extend beyond such issues nor beyond the scope of the relief demanded.*" (Emphasis added). *See, also, United Transportation Union v. State Bar of Michigan,* 401 U.S. 581 (1917); *Hedges v. Dixon County,* 150 U.S. 182, 192 (1893); *Manufacturers' Finance Co. v. McKey,* 294 U.S. 442, 451 (1935); *Steffen v. United States,* 213 F. 2d 266, 272 (6th Cir. 1954).

Nor may a court, though having obtained jurisdiction of the parties and subject matter of a cause, act in such a manner as to transcend the power conferred by the law, for when it does its judgments "would not be merely erroneous; they would be absolutely void." *Windsor v. McVeigh,* 93 U.S. 274, 23 L. Ed. 914, 917 (1874). An illegal contract once made may not be reformed. *Central Specialties Co. v. Schaefer,* 318 F.Supp. 855, 859 (N.D. Ill. 1970); *see, also, Armstrong Cork Co. v. Lyons,* 366 F.2d 206, 208 (8th Cir. 1966).

The original contracts with their illegal tying arrangements, having been violative of the Sherman and Clayton Acts, were illegal *ab initio* and were not subject to reform, and the lower courts, in reforming them and ignoring the issues at hand and scope of the relief sought, exceeded their judicial power. Such judgments are *a fortiori void.*

5. LEGAL ETHICS AND PUBLIC POLICY PRECLUDE, AND THE CONSCIENCE IS SHOCKED BY, AN *A PRIORI* WRITTEN STIPULATION IN A CLASS ACTION SETTLEMENT AGREEMENT AS TO THE AMOUNT AND MECHANICS OF DISTRIBUTION OF LEGAL FEES TO BE PAID TO PLAINTIFFS' ATTORNEYS UPON ITS APPROVAL BY THE COURT.

The precise issues raised under this Point apparently are novel and have not been subject to judicial investigation before this time, at least insofar as class action settlements are concerned. However, the courts have indicated in analogous situations that Petitioner's postulate is sound. In *Trustees v. Greenough*, 105 U.S. 527, 536, 26 L.Ed. 1157 (1881), lies the "equitable fund" doctrine, upon which the courts have grounded their allowances of legal fees to prevailing parties, although it has been recognized that an actual fund of money or monetary benefit to the prevailing party is not decisive of the issue of either the grant or amount of such fees. *Freeman v. Ryan*, 408 F.2d 1204, 1206 (D.C. Cir. 1968).

On the other hand "the practice of awarding attorneys' fees is one that has been 'delicate, embarrassing and disturbing,' for the courts." *City of Detroit v. Grinnell Corp.*, 495 F.2d 448, 469 (2nd Cir. 1974). *See, also, Milwaukee Towne Corp. v. Loew's, Inc.*, 190 F.2d 561, 569 (7th Cir. 1951), *cert. denied*, 342 U.S. 909 (1952). It is also clear that in the court, itself, is reposed the responsibility of determining the efficacy of an award and the amount thereof so as to compensate the attorney for the reasonable value of those services which benefited the claimant. *Milone v. English*, 306 F.2d 814, 819 (D.C. Cir.

1962). *See, also Sprague v. Ticonic National Bank,* 307 U.S. 161 (1939).

In exercising its discretion the trial court is not bound by agreements made between the attorney and the representative members of the class before the commencement of the suit, whether predicated upon an hourly fee basis or a contingent fee basis. *Milwaukee Towne Corp. v. Loew's, Inc., supra. See, also, State of Illinois v. Harper & Row Publishers, Inc.,* 55 F.R.D. 221, 224 (N.D. Ill. 1972).

Although the A.B.A. Code of Professional Responsibility does not contain any specific directives relating to the issue of attorney fee awards in class action settlements, the following Ethical Considerations under Canon 5 have some bearing on the question:

> "EC 5-2. * * * After accepting employment, a lawyer carefully should refrain from acquiring a property right or assuming a position that would tend to make his judgment less protective of the interests of his client."
>
> "EC 5-7. The possibility of an adverse effect upon the exercise of free judgment by a lawyer on behalf of his client during litigation generally makes it undesirable for the lawyer to acquire proprietary interest in the cause of his client or otherwise to become financially interested in the outcome of the litigation. * * *"

Petitioner submits that since the responsibility for the determination of the question of payment of fees as well as the amount of fees rests with the court and in the light of applicable ethical considerations, it is wrong to condone and approve a procedure whereby stipulations are made and agreed upon between counsel for the class and counsel for the defendant

that a specific amount will be paid as attorneys' fees; that such amount is fair and reasonable; and that such fees are to be paid by the defendant, all of which occurred in the instant case. The conclusion can best be stated in the words of the *Manual for Complex Litigation*, § 1.46, p. 57:

> "Two type of provisions in settlement agreements have appeared with sufficient frequency to warrant comment. The first is the agreement that the fees and sometimes expenses of plaintiffs' counsel are to be paid separately by the defendant(s) over and above the settlement . . . . such an arrangement should not be permitted. All amounts to be paid by the defendant(s) are properly part of the settlement fund and should be known and disclosed at the time the fairness of the settlement is considered.
>
> "The effect of such an arrangement is to neutralize the court's power and responsibility to pass upon the reasonableness of the amounts to be paid to plaintiffs' counsel since any reduction by the court in the amount counsel agree upon after the class settlement has been approved will simply go to reduce the aggregate amount of the defendant(s) will pay and will not increase the amount to be paid to the plaintiffs. As a result, there is little incentive for the judge to reduce the agreed upon fees. On the other hand, *the effect of such an arrangement may be to cause counsel for the plaintiffs to be more interested in the amount to be paid as fees than in the amount to be paid to the plaintiff.*" (Emphasis added).

Under the settlement agreement approved by the Courts below any portion of the One Million Two Hundred Fifty Thousand Dollar legal fees agreed by the Defendant to be paid to Plaintiffs' counsel that were not to be approved by the trial court would not have inured to the benefit of the Class Plaintiffs, since there is no "settlement fund" in this case but would

merely be a windfall to the Defendants. Such a result should not be condoned.

CONCLUSION

For these reasons, a Writ of Certiorari should issue to review the Judgment and Opinion of the Eighth Circuit.

Respectfully submitted,

JAY S. FICHTNER
BERMAN, FICHTNER & MITCHELL
2650 LTV Tower
1525 Elm Street
Dallas, Texas 75201
A/C 214: 748-9911
Attorneys for Petitioner

Of Counsel:
DOUGLAS E. YEAGER
2650 LTV Tower
Dallas, Texas 75201